YEARBOOK ON INTERNATIONAL INVESTMENT LAW & POLICY

2012–2013

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2012–2013

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The *Investment Yearbook* is an annual publication published by Oxford University Press in association with the Vale Columbia Center on Sustainable International Investment. It draws on the guidance of a distinguished Advisory Board, ongoing engagement by an Editorial Committee consisting of leading academics in the field of investment law and policy, and on skillful work by an Editorial Staff of students from Columbia Law School and McGill University Faculty of Law.

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Vale Columbia Center (VCC): vcc@law.columbia.edu
Andrea K. Bjorklund, Editor of the *Investment Yearbook*
andrea.bjorklund@mcgill.ca
Editorial Committee:
Abby Cohen Smutny: asmutny@whitecase.com
Lise Johnson: Ljj2107@columbia.edu
Peter Muchlinski: pm29@soas.ac.uk
Ucheora Onwuamaegbu: ucheoral@gmail.com
Federico Ortino: federico.ortino@kcl.ac.uk
Lisa Sachs: lsachsl@law.columbia.edu

CONTRIBUTORS

Björn Arp, PhD in International Law from the University of Alcalá (2006). He has been Assistant Professor of Public International Law at the University of Alcalá (2000–2010); Secretary of the LLM Program in International Human Rights Protection (2004–2010); and Visiting Researcher at Harvard Law School (2007). He has been guest lecturer at several universities in Latin America and Spain. His publications focus on the international protection of human rights and of foreign direct investments. Currently, he is Adjunct Faculty at the American University Washington College of Law and Partner at the international legal and political services firm Aparicio, Arp & Associates in Washington, D.C.

Alessandra Asteriti has degrees from the University of Rome, Essex and Glasgow, where she obtained her PhD with a thesis in international investment law. She has worked as an archaeologist in Syria and taught Italian in the United States, before moving to the United Kingdom and completing her postgraduate education in law. She is currently an affiliate researcher at the University of Glasgow. She has numerous publications in the fields of international investment law and legal theory.

Nicholas J. Birch is an Associate at the Law Offices of Stewart and Stewart in Washington, D.C. and a JD/MBA graduate from Georgetown University. Mr. Birch has practiced in trade remedies and international investment law. He has also been involved in research and writing on international investment, arbitration, and trade law and development, which has been featured in multiple books and articles.

Jenny J. Chao has experience advising international financial institutions, government, and the private sector in energy, infrastructure, natural resources management, and sustainable development, with a particular emphasis on the emerging economies in East and Southeast Asia. Previous to her current role as an associate of an international law firm, Hogan Lovells, she was a research scholar with the Vale Columbia Center on Sustainable International Investment. She holds a JD from Columbia Law School, a master's from Sciences–Po/Sorbonne, and a BS from Georgetown University's School of Foreign Service.

Hernando Diaz-Candia, Science Doctor, Universidad Central de Venezuela; *Master in Legibus* (LLM), Fulbright Scholar, Harvard Law School; abogado, *cum laude*, Universidad Católica Andrés Bello. His doctoral thesis <<*El correcto funcionamiento expansivo del arbitraje*>> was awarded highest honors and published as a book in Spain (Aranzadi-Thomson Reuters) and Venezuela (Editorial Legis) in 2011. He is authorized to practice law in Venezuela and in the State of New York. He has served as domestic and international arbitrator, including before the International Chamber of Commerce, and currently teaches arbitration as part of the Science Doctorate curriculum at Universidad Central de Venezuela. He has represented investors (claimants) and sovereign states (respondents) before ICSID.

Paolo Di Rosa is a partner at Arnold & Porter LLP, where he heads the International Arbitration Practice Group. Previously, he was a senior lawyer at the U.S. Department of State, and chief negotiator for numerous U.S. international treaties. He has been ranked or listed as an international arbitration specialist in publications such as *Chambers Global, Chambers Latin America, Chambers USA, Legal 500, International Who's Who of Commercial Arbitration, SuperLawyers*, and *Best Lawyers in America*, among others. He received an AB *magna cum laude* from Harvard College in 1987, and a JD *cum laude* from Harvard Law School in 1991.

Kabir Duggal is an associate in the International Arbitration Group at Curtis, Mallet-Prevost, Colt and Mosle LLP. He has been involved in arbitrations involving state and state-owned entities and is a graduate of the University of Mumbai, University of Oxford (Law Faculty) and the New York University School of Law.

Patrick Dumberry, PhD (Graduate Institute for International Studies, Geneva, Switzerland), is an Associate Professor at the University of Ottawa (Faculty of Law, Civil Law Section). He practiced international arbitration for several years with law firms (in Geneva and Montreal), as well as with Canada's Ministry of Foreign Affairs (Trade Law Bureau). He publishes in the fields of international law and international investment law. His publications can be found at: http://www.droitcivil.uottawa.ca/index.php?option=com_contact&task=view&contact_id=148&Itemid.

Persephone Economou is a staff member of the World Bank's Multilateral Investment Guarantee Agency (MIGA). Prior to that, she was the Managing Editor of the *Journal of International Business Studies*, where she co-edited a special issue on international business negotiations. Previously she was a staff member of UNCTAD in Geneva and of the United Nations Centre on Transnational Corporations in New York. She was involved extensively in the *World Investment Report* series and was the Associate Editor of *Transnational Corporations*. Ms. Economou has been a consultant to various organizations, including the World Bank's Development Economics.

Ksenia Gal is a Research Associate at the Vale Columbia Center on Sustainable International Investment; she holds an LLM degree in International Legal Studies from New York University Law School. Before that, she had received her first law degree from the Russian Academy of Justice in Moscow, Russia, and for several years worked at the Legal Department of the Ministry of Foreign Affairs of the Russian Federation.

David A. Gantz, AB (Harvard), JD, SJM (Stanford), is Samuel M. Fegtly Professor of Law and Director of the International Trade and Business Law Program at the University of Arizona,

James E. Rogers College of Law, where he teaches and writes in the areas of international trade and investment law, regional trade agreements, and international environmental law. He served earlier in the Office of the Legal Adviser, U.S. Department of State, and practiced law in Washington, D.C. He is the author or co-author of four books and more than 50 law review articles and book chapters, and has served as a consultant for the UNDP, USAID and the World Bank, among others.

Caroline Henckels holds a PhD from the University of Cambridge, an LLM from the University of Melbourne and an LLB from Victoria University of Wellington. She is a Barrister and Solicitor of the Supreme Court of Victoria, Australia and of the High Court of New Zealand. She currently holds the position of Vice-Chancellor's Postdoctoral Research Fellow at the University of New South Wales, Australia. A monograph based on her PhD thesis, which concerns proportionality and standards of review in investor-state arbitration, will be published by Cambridge University Press in 2015.

Dawn Yamane Hewett is an associate in Arnold & Porter LLP's international arbitration, litigation, global anticorruption, and white collar practice groups. Ms. Hewett's practice includes the representation of sovereign states, corporate clients, and individuals in international arbitrations, U.S. litigation, and U.S. criminal investigations. Ms. Hewett obtained her JD from Yale Law School in 2008, Master's of Public Affairs from Princeton University in 2005, Master of Philosophy in Ethnic and Racial Studies (Sociology) from Trinity College Dublin in 2002, and undergraduate degrees in International Studies and Political Science from the University of Washington in 2000.

Lise Johnson is the Senior Legal Researcher on Investment Law and Policy at the Vale Columbia Center on Sustainable International Investment (VCC), where she focuses on analyzing treaties and treaty-based investor-state arbitrations, and examining the implications those instruments and decisions have for host countries' domestic policies and development strategies. In addition, she concentrates on key institutional and procedural aspects of the legal framework government resolution of investor-state arbitration, including efforts to increase transparency in and legitimacy of investor-state dispute settlement. She has a BA from Yale University, JD from University of Arizona, LLM from Columbia Law School, and is admitted to the bar in California.

Ian A. Laird is a Partner in the International Dispute Resolution group of Crowell & Moring LLP, based in the firm's Washington, D.C. office. He has served as a Lecturer-in law at Columbia Law School and as an Adjunct Professor at the Georgetown University Law Center teaching subjects related to international investment law. He is Editor-in-Chief and Co-Founder of *Investmentclaims.com* (Oxford University Press), and Co-Director of the International Investment Law Center of the International Law Institute (ILI) in Washington, D.C. He has appeared as counsel in numerous investor-state arbitrations. For more information, see: http://www.ianlaird.com.

Shawn Lim is Managing Editor of the *Columbia FDI Perspectives* and Fellow at the Vale Columbia Center on Sustainable International Investment. He is currently a JD candidate and Harlan Fiske Stone Scholar at Columbia Law School. He is also Articles Editor of the *Columbia*

Journal of European Law and holds an LLB with First Class Honours from the London School of Economics and Political Science.

Jo En Low is an associate at Clifford Chance LLP. She specializes in cross-border M&A in the energy, infrastructure and telecommunications sectors. Her research interests include foreign direct investment and international development. Ms. Low is a graduate of Columbia Law School and the University of New South Wales. She was formerly a research associate to the Vale Columbia Center on Sustainable International Investment and the Harvard Kennedy School Corporate Social Responsibility Initiative. As a student, Ms. Low was a staff editor of the Columbia Journal of Transnational Law and has published on subjects such as state-controlled entities, international investment, business and human rights.

Rahim Moloo *(at the time of writing)* was General Counsel at the University of Central Asia, an international treaty organization, and Senior Research Fellow at the Vale Columbia Center on Sustainable International Investment. Since then, Mr. Moloo joined Freshfields Bruckhaus Deringer LLP as a Senior Associate in the International Arbitration Group. He has extensive experience in representing and advising multinationals, states and international organizations on matters of international law and in international disputes. In particular, Mr. Moloo focuses on representing parties in international investment disputes and international commercial arbitrations. Concurrently, Mr. Moloo is an adjunct professor at Columbia Law School, where he teaches a seminar on international commercial arbitration.

Vid Prislan is Research Fellow and PhD candidate at the Grotius Centre for International Legal Studies, Leiden University. He holds a diploma in international relations from the University of Ljubljana, and an LLB in Dutch law and LLM (*cum laude*) in public international law from Leiden University. In addition to conducting doctoral research on the interaction between domestic courts and investment tribunals, he regularly provides expert advice to governments and private parties in territorial and maritime delimitation disputes, and in the context of various investment arbitration proceedings. He is also Book-Review Editor of the Leiden Journal of International Law. Previously, he worked as research assistant at the Grotius Centre and supported counsel in contentious cases before the PCA and the ICJ.

Borzu Sabahi is an attorney in Curtis Mallet-Prevost Colt & Mosle LLP. He represents states and state-owned entities in complex commercial and investment treaty arbitrations under the rules of ICC, ICSID, LCIA, and UNCITRAL involving industries such as oil and gas, mining, construction, and telecommunications. He is an adjunct professor at Georgetown and Columbia Law Schools where he co-teaches seminars on investor-state arbitration and on international oil and gas development. He is co-director of the International Investment Law Center at the ILI and an editor of Oxford's Investment Claims website. He has widely published on international investment law and arbitration and regularly speaks at professional conferences on these topics.

Lisa Sachs is the Director of the Vale Columbia Center on Sustainable International Investment. At the VCC, she has overseen the development of robust research portfolios and advisory work on sustainable investment in natural resources (oil, gas, mining, and land) and international investment law and policy. Her academic work has included research on extractive industries, trends in foreign investment, corporate responsibility, human rights, and integrated economic development. She is a member of the UN Sustainable Development Solutions Network thematic group on the Good Governance of Extractive and Land Resources. She received a BA

from Harvard University and a JD and a Master of International Affairs from Columbia University, where she was a James Kent Scholar and recipient of the Parker School Certificate in International and Comparative Law.

Mavluda Sattorova is a lecturer at the University of Liverpool School of Law where she teaches courses in international investment law, international energy law and law of the WTO. Prior to obtaining her PhD and LLM degrees from the University of Birmingham, she completed a PhD in civil law (Tashkent State Institute of Law) and taught at the National University of Uzbekistan. She was admitted to the Uzbek Bar in 1999 and was involved in drafting and negotiating investment contracts and representing clients before the Supreme Economic Court of Uzbekistan.

Karl P. Sauvant is Resident Senior Fellow at of the Vale Columbia Center on Sustainable International Investment (VCC–a joint center of Columbia Law School and The Earth Institute at Columbia University), Senior Research Scholar and Lecturer in Law at Columbia Law School and Guest Professor at Nankai University, China. Before that, he was the Founding Executive Director of the VCC and Director of UNCTAD's Investment Division. He is a Fellow of the Academy of International Business and an Honorary Fellow of the European International Business Academy. He received his PhD from the University of Pennsylvania in 1975.

Stephan Schill (Dr. iur. (Frankfurt), LLM. (NYU), LLM. (Augsburg)) is Senior Research Fellow at the Max Planck Institute for Comparative Public Law and International Law in Heidelberg, Principal Investigator of the ERC-project on "Transnational Public-Private Arbitration as Global Regulatory Governance," and Lecturer at the Frankfurt University and in the joint LLM program of Heidelberg University and the Universidad de Chile. He is admitted to the bar in Germany and New York and has acted as counsel before the European Court of Human Rights. He is also the Editor-in-Chief of the Journal of World Investment and Trade.

Jacob Stone LLB (civil law, Université Laval), JD (common law, magna cum laude, University of Ottawa), is a lawyer at McCarthy Tétrault LLP in Québec City, Canada. A member of the firm's Business, Mining and International Trade and Investment Law Groups, his practice focuses on corporate and project financing, securities, mergers and acquisitions and venture capital in the mining, energy and biotechnology sectors as well as investment treaty and foreign corruption issues. The views expressed herein are his own and do not necessarily reflect the views, positions, or opinions of McCarthy Tétrault LLP on such matters. Before joining McCarthy Tétrault LLP, Mr. Stone worked in international arbitration in the investment and services section of the Trade Law Division of the federal Department of Foreign Affairs, Trade and Development in Ottawa, Canada.

Witold P. Wilinski is Assistant Professor at the Warsaw School of Economics (World Economy Faculty) where his work focuses primarily on international investment and emerging market multinational enterprises. He was a Visiting Researcher at the Vale Columbia Center on Sustainable International Investment at Columbia University. He received his PhD from the Warsaw School of Economics and a Post-Master Diploma from University Paris Dauphine.

Ruben Zandvliet is a PhD candidate at the Grotius Centre for International Legal Studies, Leiden University. His research focuses on labor standards in international economic law. He

holds an LLM (*cum laude)* from Leiden University and an LLM (*James Kent Scholar*) from Columbia University. In addition to his doctoral studies, he is a visiting researcher at The Hague Institute for Global Justice. Previously, he worked as a policy adviser for a Member of Parliament in the Netherlands in the field of economic policy, corporate law, and constitutional law.

12 June 2013
Investment Yearbook 2012–2013

FOREWORD

The international investment law and policy regime has developed rapidly over the past four decades and, in the process, undergone considerable changes. As Jeswald W. Salacuse and Nicholas P. Sullivan observed when writing about the regime as it existed in the mid-1970s: "foreign investors who sought the protection of international investment law encountered an ephemeral structure consisting largely of scattered treaty provisions, a few questionable customs, and contested general principles of law."[1] Today, the investment regime is stronger than it has ever been in terms of protecting foreign investors. In fact, the investor-state dispute-settlement mechanism arguably makes it stronger than the international trade regime.

Partly because of this rapid development of the investment regime, it is far from perfect. As Brigitte Stern suggested several years ago, the regime was undergoing a "*crise de croissance*, a teenager's crisis," although she updated her observation in 2013 to say that "the teenager is now in his twenties and should become more reasonable. In fact, in my view, he does."[2] Certainly, more countries are strengthening the regime by entering into new international investment agreements and accepting its functioning, thus firming it up, than are leaving the regime or seriously questioning key aspects of it (including its dispute-settlement mechanism), thus diminishing its legitimacy.

This state of affairs is not surprising: Like any regime, the international investment regime is in constant evolution. All stakeholders and others who have an interest in the investment regime – governments, business, trade unions, local communities, nongovernmental organizations, practitioners, academics – contribute to this evolution in one way or another, either by changing the regime's substantive and procedural provisions or by advocating various changes – some small, some big. Some of the proposed changes would strengthen the protection of foreign investors and investments, some seek greater liberalization, some aim for a new balance between the rights and obligations of governments and investors, some want to emphasize the right to

1. Jeswald W. Salacuse and Nicholas P. Sullivan, "Do BITs Really Work? An Evaluation of Bilateral Investment Treaties and Their Grand Bargain," 46(1) *Harvard International Law Journal* 67 (2005), p. 68.

2. "An interview with the Honorable Charles N. Brower and Professor Brigitte Stern," *Arbitration Trends*, Winter 2013, p.13.

regulate, and some seek a reorientation of the purpose of the regime. Other proposed changes relate to procedural matters and, especially, the dispute-settlement mechanism. However, virtually all proposed changes reflect the recognition that international investment needs a strong rule of law; debated is what, precisely, that rule of law should encompass and how it should be implemented, in the interest of strengthening the legitimacy of the international investment regime and in light of changing circumstances and new realities.

Among the new realities, none is more important than the growing number of emerging markets (all non-OECD countries) that are becoming significant outward investors. During the period 2007–2011, at least 129 emerging markets reported outward foreign-direct-investment transactions; outflows from these economies reached US$ 460 billion in 2011 – some nine times world outflows during the first half of the 1980s.[3] Emerging markets have become important participants in the world foreign-direct-investment market. This gives especially the most important among them (including the BRICs) a different stake in the international investment law and policy regime. It is a stake that is no longer almost exclusively defined by their position as capital-importing *host* countries, but increasingly also as capital-exporting *home* countries, interested in protecting their investments abroad and facilitating the operations of their investors. Conversely, the traditional home countries, the developed countries, are increasingly "discovering" that they are also important host countries, interested in maintaining their own policy space to pursue legitimate public policy objectives. Moreover, governments in both groups of countries have become respondents in a growing number of investment disputes; and the potential for such disputes is very high, considering that there are more than 100,000 multinational enterprises that control over one million foreign affiliates, in a world in which the great majority of countries are bound by international investment agreements that typically include investor-state dispute-settlement provisions.

This fundamental shift in the interest situation of a growing number of countries toward mixed interests as home and host countries may lead to a narrowing of differences (and perhaps even a convergence of interests) between the traditional host and home countries that, eventually, may allow a multilateral investment regime to emerge. But we are certainly still quite far from such a regime. At the same time, though, the series of bilateral and regional investment negotiations among major countries that are underway could potentially further narrow the differences in various approaches, yielding perhaps a template that could become the guidepost for future common efforts.

In this rapidly evolving setting, myriad issues emerge that require the attention of scholars, practitioners, investment negotiators, business executives, trade-union officials, members of nongovernmental organizations, and other interested parties. This edition of the *Investment Yearbook* offers, as in the past, a platform for the examination of the various aspects of the international investment problématique, with a view toward reaching a better understanding of the subject matter. All of the authors who contributed to it have taken full advantage of this opportunity. Particularly noteworthy is that the present edition pays special attention, in the context of its Symposium, to issues relating to sustainable international investment. This is important and timely, as the ongoing discussions about improving the international investment law and policy regime need to include, if not to start from, a review of the purpose(s) that the regime is meant to serve. Everything else – including its substantive content and it procedural mechanisms – flows from the purpose(s) of the regime.

3. UNCTAD, *World Investment Report 2012* (Geneva: UNCTAD, 2012).

I congratulate the new Editor of the *Investment Yearbook* and the members of its Editorial Committee for this edition of the *Investment Yearbook* and wish them every success for future editions.

Karl P. Sauvant, PhD
Founding Editor of the *Investment Yearbook*
Resident Senior Fellow
Vale Columbia Center on Sustainable International Investment

PREFACE

Investment law continues to grow at an extraordinary pace and to attract attention and criticism from its proponents and its opponents, and from those who lie somewhere in between. The 2012–2013 *Yearbook* reflects the wide-ranging nature of investment law and its inviolable links with policy, with topics that include questions about applicable law and the interplay between multiple potentially applicable laws, the challenges inherent in negotiating a regional trade agreement among states with divergent levels of economic development, the effect of states' policies to encourage *outward* foreign direct investment that distorts the competitive relationship among investors, and the effect that sustainable development concerns have, and ought to have, on international investment law. Given this breadth, it is challenging to identify unifying themes. Yet there are some observations that draw together the eclectic and rich contributions to this edition of the *Yearbook*.

First, the range of people interested in investment law is remarkable. The authors in the *Yearbook* range from seasoned practitioners to junior academics, from policy experts to crackerjack lawyers, and from public international law specialists to private international law mavens. Investment law attracts people with divergent international interests and areas of expertise and provides them with a large forum in which to interact.

Second, notwithstanding concerns about the fragmentation of international law, investment law is arguably a counterexample to the fragmentation dynamic. While investment lawyers are specialized, and investment case law continues to grow and can be self-referential, investment law does look outside itself for guidance and influence. Topics such as the intersection of investment law and sustainable development law, covered in the *Yearbook*'s virtual symposium, the intersection of investment law with municipal laws and the intersection of domestic contract law with international law, covered in two of the *Yearbook*'s chapters, show the vibrance of investment law and the potential for it to be influenced by other legal regimes, instead of operating in splendid isolation.

Third, the appropriate role of state-owned or state-controlled enterprises (SCEs) is central in one contribution, and subsidiary in at least two others. This includes questions about whether SCEs can be claimants as well as whether they can be respondents in investor-state arbitration cases – inverse questions that demonstrate the reach and complexity of the investor-state dispute settlement regime – as well as concerns about the influence that states may exert over

the investment decisions of SCEs and the concomitant effect of those decisions on competitive neutrality.

Fourth, notwithstanding concerns about investment agreements generally and investor-state dispute settlement in particular, and notwithstanding some diminution in the number of investment agreements signed every year, many states continue to pursue an energetic negotiating agenda. The United States is one of the more active, and the Trans-Pacific Partnership, if achieved, will likely point the way to what we might expect from the even more ambitious Transatlantic Trade and Investment Partnership (TTIP) – the proposed agreement between the European Union and the United States. The release of a new U.S. Model BIT in 2012, while disappointing to many (including both those who sought stronger protections for business and those who sought greater regulatory autonomy for host states) can be viewed as an endorsement of the status quo, though with some slight changes likely to be of importance particularly in negotiations with China and India.

The *Yearbook* of 2012–2013 starts with its customary survey of the "state of the world" in three areas of international investment law: trends in foreign direct investment; notable events in arbitration jurisprudence; and the ways that states are reforming international investment agreements as they react to developments in cases and practice. Taken together, these three pieces provide a comprehensive review of the state of international investment law and policy underpinned by expert analysis and commentary.

Investment commentary sometimes focuses more on law than on policy. Yet the raison d'être of international investment agreements is to promote foreign investment (not just to provide protection to those investments). Thus, the first piece in the *Yearbook*, written by Karl P. Sauvant, Persephone Economou, Ksenia Gal, Shawn Lim, and Witold P. Wilinski, begins by describing and assessing trends in foreign direct investment in 2012. Foreign direct investment decreased in 2012, after a modest increase in 2011. It then turns to an understudied but increasing area of concern in investment policy – home country measures (HCMs), which influence and often direct investment flows to certain destinations. These measures have an effect on "competitive neutrality" by affecting companies' decisions about where to invest and even about whether to invest; some measures effectively subsidize outward foreign direct investment so long as it is directed in particular ways. The authors provide a detailed survey of HCMs in the top ten developed countries and the top ten emerging markets (as measured by UNCTAD) and thoughtful, cogent analysis of the potential effects of those measures on investment decisions and the policies that home countries seek to effectuate with the establishment of measures that encourage and direct investment.

Dispute settlement is a key feature of investment law, and the second piece, written by Ian A. Laird, Borzu Sabahi, Frédéric G. Sourgens, Nicholas J. Birch, and Kabir Duggal, is a comprehensive, insightful assessment of 2012's investment jurisprudence. It covers the jurisdictional issues ever present in international investment law, including the effect of EU membership on Energy Charter claims, the requirement that an investor have made an "investment" and associated difficulties therein, and MFN clauses. The authors include description and analysis of tribunals' treatment of burden of proof. As for merits issues, the authors cover several umbrella clause cases, along with claims of violations of fair and equitable treatment and expropriation without payment of compensation and one case involving performance requirements. The chapter also addresses matters such as the principle of judicial economy, the overlap and conflation of various obligations, and evidentiary burdens regarding the establishment of liability. The final section covers compensation and nonpecuniary awards, with in-depth analysis of the valuation methods employed by tribunals in multiple contexts.

One of the most important sources of states' current views on investment policy, on the laws that facilitate investment, and on dispute settlement is their current investment agreements. The third chapter in Part One surveys the investment agreements signed by states in 2011 and 2012. The authors, Lise Johnson and Lisa Sachs, discern several trends of interest to the investment law community: developments in the balance of power between states and tribunals; fewer inclusions of "umbrella clauses" in treaties; greater attention to the interaction between investment law and labor and environmental concerns; a growing number of countries including transparency provisions in their treaties (although the majority of agreements still do not include transparency provisions); and issues surrounding termination, renewal, and renegotiation of treaties as many agreements near the end of their initial life-span, often a period of ten years. The authors conclude by bringing their expertise to bear by providing in-depth analysis of three important agreements in the investment realm: the Southern African Development Community's proposed Model Investment Agreement for use by its members (which, inter alia, recommends against the inclusion of a fair and equitable treatment obligation and investor-state dispute settlement), the European Union's proposals regarding investment policy, and the United States' 2012 Model BIT (which is covered in less detail given the chapter devoted to it later in the volume).

Part Two of the *Yearbook* commences with a symposium, expertly directed by Lise Johnson and Rahim Moloo, on the intersection between sustainable development and international investment law. An impressive and wide-ranging array of chapters includes one by Rahim Moloo and Jenny J. Chao, discussing strategies for ensuring that sustainable development principles inform and guide the application and development of investment law and a contribution by Caroline Henckels on the role that deferential standards of review play in that regard. Stephan W. Schill discusses in his chapter the importance of treating international investment law as part of the international law of development rather than as antagonistic towards it. Vis Preslan and Ruben Zandvliet offer their perspective on the prospects for incorporation norms of corporate social responsibility in international investment agreements. Mavluda Sattorova discusses the intersection of international investment law and renewable energy, with a comparative analysis of EU law and international trade law to illustrate that existing investment law may leave too little space for national policy initiatives regarding green energy. Finally, Alessandra Asteriti addresses the perennially fertile topic of regulatory expropriation.

The chapters in Part Three illustrate the eclectic and broad reach of international investment law. Two chapters address different facets of the ever-present and ever-difficult issue of applicable law. The first of these, by Patrick Dumberry and Jacob Stone, analyzes tribunal practice in choosing the law applicable to state contracts in arbitrations convened under the ICSID Convention. In addition to providing a thorough assessment of tribunal practice with respect to contractual claims, as opposed to BIT claims, the chapter engages with the important policy question of what role, if any, international law should play when state contracts are governed by municipal law, usually that of the host state. They conclude that international law is not limited to playing a corrective or complementarity function, even when a contract contains an explicit choice-of-law clause, but that at the very least the customary international law principle of minimum standard of treatment should be held to apply in all cases. The second chapter on applicable law, by Hernando Diaz-Candia, addresses what might be described as the inverse question: What role should municipal law play in an international investment arbitration and, in particular, what role does municipal law play in establishing whether there has been a breach of an investment treaty obligation or of customary international law? He suggests that tribunals should take a deferential view when states are consistently applying municipal laws of general applicability, but that deference should be *less* in the case of individualized decisions; in any

event, the burden should rest on the investor to prove a breach of international law, with a presumption of the lawfulness of state activity.

In the next chapter Jo En Low offers an empirical assessment of the ways that investment agreements treat state-controlled entities (SCEs). For this novel and thorough chapter she reviewed 851 treaties in the course of her research, which represented treaties covering 70 percent of foreign direct investment outflows for the period 2005–2010. Ms. Low concludes that while some treaties (particularly those concluded by the United States, by Japan after 2002, and by many Middle Eastern states) explicitly include state-controlled entities in their definition of investor, most do not explicitly address whether SCEs may qualify as investors (and thus as claimants) under the treaty. Yet the definition of investor in most treaties is broad enough to allow SCEs to qualify, subject to its meeting all necessary requirements, which Ms. Low carefully and clearly details. In a few rare treaties SCEs are explicitly excluded. Ms. Low then addresses whether an SCE might have difficulty commencing an ICSID Convention–based arbitration if the SCE is treated as the *state* itself, rather than as a *national* of the state, but concludes that such an outcome is neither desirable nor mandated by the negotiating history of the ICSID Convention or by the evolution of the meaning of "national" in international law.

The *Yearbook* then turns to chapters analyzing two investment agreements of likely historical importance. David A. Gantz offers his assessment of the Trans-Pacific Partnership (TPP), a proposed multilateral free trade agreement whose current members just completed (in August 2013) their 19th round of negotiations. Professor Gantz particularly analyzes the TPP as a key part of the United States' political, military, and economic strategy in Asia. The TPP is currently projected to include a chapter on investment and resolution of disputes through investor-state dispute settlement (although Australia's previous government, under Prime Minister Julia Gillard, announced that Australia would no longer sign agreements that provide for investor-state arbitration; it is not clear whether the current government will continue that policy or whether Australia would be able to impose that policy on the other member states), and Professor Gantz's analysis covers those issues as well as other potentially difficult issues such as the treatment and responsibilities of state-owned enterprises, the treatment of tobacco products, the scope of intellectual property protections, the position of labor and environmental protections, market-access issues, and required transparency of regulatory measures. He assesses the hurdles that must be overcome before the TPP negotiations can be concluded.

The year 2012 saw the belated issuance of a new U.S. Model BIT. Paolo Di Rosa and Dawn Y. Yamane Hewett, noting first that the 2012 Model BIT is a bit anticlimactic given that it did not depart significantly from its predecessor, provide an overview of what did and did not change in the new model. As to the former, the new BIT proposes more significant obligations regarding regulatory transparency, expands obligations to protect labor and the environment, ensures that SOEs are subject to the same standards as states themselves when they are acting under delegated governmental authority, contains revisions to financial services regulations, and clarifies that the definition of "territory of a Party" includes the territorial sea. Mr. Di Rosa and Ms. Hewett then analyze the likely effects of these changes on future BIT negotiations with such likely treaty partners as China, India, and Russia, among others.

The final chapter is a contribution by Björn Arp on the regulation of foreign direct investment in Bolivia. This short case study outlines the state of affairs in Bolivia after its renunciation of the ICSID Convention in 2007 and the renunciation of several of its BITs. Bolivia also adopted a new constitution in 2009, which provides, inter alia, that domestic law has precedence over international law. Bolivia has also given notice of termination of several of its BITs. It is thus in the vanguard of the backlash against international investment law and arbitration and its assertion of the primacy of state control over natural resources does not permit foreign investors to

have much negotiating leverage. Mr. Arp's case study describes a "natural resources naturalism" that allows room for arbitrary governmental decision-making and corruption.

The volume closes with the customary inclusion of the best memorials submitted by contestants in the FDI Moot Competition. The winning memorial for claimants was submitted this year by students from the Nalsar University of Law in Hyderabad, India, and the winning memorial for respondents was written by students from Saint Petersburg State University in Russia. The FDI Moot's popularity, and the number of students participating, has been growing every year. These memorials won amidst stiff competition and signal the breadth and the depth of those devoting their attention to investment law.

Andrea K. Bjorklund
L. Yves Fortier Chair in International Arbitration and International Commercial Law
McGill University Faculty of Law

Lise Johnson
Senior Legal Researcher: Investment Law and Policy
Vale Columbia Center on Sustainable International Investment

Peter Muchlinski
Professor of International Commercial Law, The School of Law, The School of Oriental and African Studies, University of London

Ucheora Onwuamaegbu
Legal Adviser, Kuwait National Focal Point

Federico Ortino
Reader in International Economic Law
School of Law
King's College London

Lisa Sachs
Director
Vale Columbia Center on Sustainable International Investment

Abby Cohen Smutny
Partner, White & Case LLP, Washington, D.C.